IN THE HIGH COURT OF JUDICATURE AT MADRAS

Dated : 29.10.2007

Coram :

THE HONOURABLE MR.JUSTICE K.RAVIRAJA PANDIAN
and
THE HONOURABLE MRS.JUSTICE CHITRA VENKATARAMAN

Tax Case (Appeal) Nos.1361 and 1362 of 2007

Commissioner of Income Tax,
Chennai. .. Appellant in both appeals

versus

M/s.Vinbros and Company,
No.23, Romain Rolland Street,
Pondicherry. .. Respondent in both appeals

Appeals preferred under section 260-A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, Madras 'C' Bench dated 23.02.2007 in ITA No.2019/Mds/06 and ITA.No.2020/MDS/06 against the order ITA.Nos.517 & 518/05-06 and ITA.Nos.206 & 207/06-07 dated 17.08.2006 Assessment years of 2003-04 & 2004-05 on the file of Commissioner of Income Tax (Appeals) XI, Chennai.

Against the order PA.No/GI.No.AAAFV0610R/4301V dated 13.03.2006 Assessment years 2003-04 and 2004-05 on the file of the Income Tax Officer Ward I(1) Pondicherry.

For Appellant : Mr.J.Narayanasamy,
Jr. Standing Counsel for IT Department

JUDGMENT

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(Judgment of the Court was delivered by CHITRA VENKATARAMAN, J.)

This appeal is filed by the revenue seeking admission by framing the following question of law :

"Whether on the facts and circumstances of the case, the Tribunal was right in holding that blending and bottling of IMFL would amount to 'manufacture' for the purpose of claiming deduction under Section 80-IB?

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2. The assessee herein is small scale industry recognised as so by the Director of Industries, Pondicherry. It set up a second unit to manufacture and bottle Indian manufactured foreign liquor (IMFL) at Pondicherry. In its return for the assessment year 2003-04 and 2004-05, it claimed deduction under Section 80-IB of the Act in respect of the profits and gains derived from the second unit. The assessing officer however rejected the plea on the issue that the process carried on by the assessee for its product does not constitute 'manufacture' within the meaning of Section 80-IB of the Act. He further held that setting up of the second unit is only an expansion or reconstruction of the existing unit. Aggrieved by the same, the assessee preferred an appeal before the Commissioner of Income Tax (Appeals).

3. In the proceedings before the Commissioner of Income Tax (Appeals), the assessee explained the process of blending as follows:

The assessee purchased rectified spirit or extra neutral alcohol (ENA) made of grain or grapes or malt to which it added demineralised water in required proportion to reduce the strength of the ENA to make various products like whiskey, brandy, rum, etc. Apart from that, other ingredients like caramel, sugar etc., were also added as per blending formulations. This blend was subject to filtration for required time, blend inspection and then bottling in empty bottles. The finished products were packed and sold.

4. The Commissioner of Income Tax (Appeals) considered the fact that the alcoholic strength of ENA which was around 95% v/v was reduced to a maximum of 42.8% v/v. Consequently, the Commissioner of Income Tax (Appeals) held that there was no manufacture or production of any new article or thing as the alcohol which was the input remained as alcohol. In the circumstances, he rejected the plea for deduction under Section 80-IB of the Act.

5. On further appeal before the Tribunal, the assessee reiterated the contentions as regards the process undertaken to result in a totally different marketable commodity. Considering the entirety of the issue and applying the decision of Allahabad High Court in the case of CIT v. Rampur Distilleries and Chemicals Company Ltd., reported in 277 ITR 416, the Tribunal held that the rectified spirit is not mentioned in the 1st Item of 11th Schedule "beer, wine and other alcoholic spirits" and consequently, the assessee as a Small Scale Industrial Unit was entitled to deduction under Section 80-IB of the Act. Aggrieved by that order, these appeals are filed.

6. Learned counsel for the Revenue submitted that considering the fact that what was purchased was a concentrated form of rectified spirit and what has been sold is only a diluted form, there is no manufacturing process to result in a different commodity for the purpose of claiming deduction under Section 80-IB of the Act. Learned counsel referred to the 11th Schedule to the Act under which aerated water with further additions were made in the form of essence, was not taken as an item of manufacture to grant the relief under Section 80-IB of the Act. In the

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circumstances, referring to the said Section, learned counsel submitted that the assessee has not manufactured an item to have the benefit of deduction under Section 80-IB of the Act. He also pointed out that the assessee cannot claim deduction under Section 80-IB of the Act in respect of the items manufactured as referred to in the list in the 11th Schedule. He referred to the decision of the Karnataka High Court in the case of State of Karnataka Vs. Shaw Wallace & Co. Ltd. reported in 110 STC 507 in support of his contention that unless and until the assessee is able to show what had been undertaken viz., blending amounted to manufacture, claiming the relief under Section 80 IB of the Act does not arise.

7. We do not agree with the submission of the learned counsel for the Revenue. A perusal of Section 80-IB shows that a deduction under the said provision is available only where the assessee engages in the manufacture or production of an article or thing, not being an article or thing as specified in the list in the 11th schedule or operates one or more cold storage plant or plants in any part of India. The proviso to sub-clause (iii) of sub section (2) of Section 80-IB of the Act shows that the condition with reference to the list in the 11th Schedule does not apply at all to the case of an industry being a small scale undertaking or an undertaking referred to in sub-section (4). The industry run by the assessee is admittedly a small scale industry, reference to 11th Schedule for the purpose of consideration of the claim under Section 80-IB of the Act does not arise.

8. As regards the second issue as to whether the assessee had engaged itself in the manufacturing or producing of an article of thing by the act of blending, it is seen that the assessee does not just add water and sells the final product. It is an admitted fact that quite apart from water, the assessee had to add several items to make it fit for human consumption. This is elaborately discussed in the order of the Commissioner of Income Tax (Appeals) which is as follows:

> " The unit manufacturing IMFL is recognized as an industry engaged in an activity of manufacture or production of an article under different statutes. There are various licences and permissions that are required for setting up and operating an industrial unit for the manufacture of IMFL. As many as 10 of such licences and permissions were listed by the appellant. Further that the Bureau of Indian Standards had laid down specifications for IMFL industry, it has been stated. It was stated that the process of blending requires special environment by use of expensive equipment with skilled labour. Apart from alcohol, even water, which is produced in house has to be not only potable but also suitable for the purpose. The other materials used are neutral alcohol, malt spirit, grape spirit, caramel, sugar, dissolvent etc to be used at a particular temperature and filtered to the special filteration and such other processes. "

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The Commissioner of Income Tax (Appeals) also pointed out that the assessee was bottling IMFL of various brands of various distilleries. The Commissioner noted that the assessee was merely blendingand bottling these brands. The admitted facts relating to the process as stated in the Commissioner's order shows that the assessee was not a manufacturer of ENA which was the basic raw material required for making various IMFL products. Instead it was only mixing water and other ingredients with ENA formulations. In the process, the alcoholic strength of the ENA which was around 95% v/v was reduced to a maximum of 42/8% v/v as in respect of whiskey, brandy, rum, vodka and gin. However, the Commissioner held that there was no manufacture or production of any new article or thing as the alcohol which was the main input, remained as alcohol. The Commissioner, however, rejected the claim on this view that there was no manufacture. The Tribunal, in its order, has stated that the blending was subject to filtration for required time and thereafter only, the final product was sold. It is also stated that the alcoholic strength of the ENA was reduced considerably to more than 50% to result in a final marketable commodity. On the face of the facts stated above, it is not possible for us to accept that the blending should not be treated as a manufacturing activity under Section 80-IB of the Act.

9. Learned counsel for the Revenue submitted that what had been undertaken by the assessee was only part of the manufacture and that every process would not amount to manufacturing. The process undertaken did not result in a totally different commodity and the input remained the same even after processing and consequently, there is no justification in granting the benefit.

10. The Tribunal referred to the decision of the Supreme Court in the case of Aspinwall & Co. Ltd. v. CIT (2001) 251 ITR 323, with regard to the concept of what would amount to manufacture. It referred to the decision in the case of Deputy Commissioner of Sales Tax Vs. PIO Food Packers reported in 46 STC 63 (SC) wherein it was observed that the test for determination whether manufacture can be said to have taken place is whether the commodity which is subject to the process of manufacture can no longer be regarded as the original commodity, but it is recognised in the trade as a new and distinct commodity. It was observed at page 65 in the decision reported in 46 STC 63 (SC) (Deputy Commissioner of Sales Tax Vs. PIO Food Packers) as follows:

> " Commonly, manufacture is the end result of one or more processes through which the original commodity is made to pass. The nature and extent of processing may vary from one case to another, and indeed there may be several stages of processing and perhaps a different kind of processing at each stage. With each process suffered, the original commodity experiences a change. But it is only when the change, or a series of changes take the commodity to the point where commercially it

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can no longer be regarded as the original commodity but instead is recognised as a new and distinct article that a manufacture can be said to take place. "

11. Following the same, the Tribunal held that what was purchased by the assessee was not a potable one and but for the blending, the commodity could not have become a saleable commodity. Consequently, the raw materials, even though are not manufactured by the assessee, yet there is nexus of the process by blending to make it a saleable commodity totally different from that of the original obtained. The Tribunal also referred to the decision of this Court in CIT Vs. PREMIER TOBACCO PACKERS P. LTD. reported in 284 ITR 222 and the decision of the Supreme Court in the case of CIT Vs. BUDHARAJA & CO. reported in 204 ITR 412 and held that the assessee was entitled to the relief under Section 80-IB being small scale industry engaged in the production of IMFL from rectified spirit. The Tribunal also pointed out that the end product is totally different and is commercially different commodity than the major input rectified spirit, which is not fit for human consumption. Hence, the changes made to the original product results in a new different commodity, which is recognised as to in the trade.

12. In Aspinwall & Co. Ltd. Vs. CIT reported in (2001) 251 ITR 323, the Apex Court, while considering the question of investment allowance, in the case of curing of coffee, considered whether the manufacturing of coffee beans would amount to manufacturing activity, and held that the word 'manufacture' has not been defined in the Income Tax Act, 1961. The Supreme Court held that the word "manufacture" has to be given a meaning as is understood in common parlance. The Apex Court held at page 327 as follows:

" It is to be understood as meaning the production of articles for use from raw or prepared materials by giving such materials new forms, qualities or combinations whether by hand labour or machines. If the change made in the article results in a new and different article then it would amount to a manufacturing activity. "

The Apex Court pointed out to the various processes and held that conversion of the raw berry into coffee seeds was a manufacturing activity; that coffee bean had an independent identity from the raw material i.e., berry from which they were produced. Considering the various process involved, the Supreme Court held that the assessee was entitled to investment allowance under Section 32-A. The Apex Court held that "if a commercially different article or commodity results after processing, then it would be a manufacturing activity. "

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13. While dealing with the question as to whether the processes of bleaching, dyeing, printing, sizing, shrink proofing, water proofing rubberising or organic processing carried on in respect of cotton or man made grey fabric amounted to 'manufacture' within the meaning of Section 2(f) of the Central Excise and Salt Act, 1944, the Apex Court, in the decision reported in 179 ITR 317 (UJAGAR PRINTS Vs. UNION OF INDIA), held that the generally accepted test to find out whether there was manufacturing was to see whether the application of processes brought out a change to take the commodity to a commercially different and distinct commodity that it could no longer be considered as the original commodity. The said decision was applied in 251 ITR 323 (ASPINWALL & CO. LTD. Vs. CIT) and again by the Apex Court in (2006) 12 SCC 468 (ORIENT PAPER & INDUSTRIES LTD. Vs. STATE OF M.P.). The law thus declared when applied to the facts herein, show that the end product is commercially different from the rectified spirit which is not fit for human consumption. The Tribunal, as a final fact finding authority, held that the changes made to the original product results in a different commercial commodity recognised as to in the trade. It may be seen that the assessee placed reliance on the decision reported in (1990) 1 SCC 109 (SYNTHETICS AND CHEMICALS LTD. Vs. STATE OF U.P.). At paragraph 74 of the said decision, the Apex Court referred to the ISI specifications dividing ethyl alcohol into several kinds of alcohol. It also pointed out as follows:

> " It appears, therefore, that industrial alcohol which is ethyl alcohol (95 per cent) by itself is not only non-potable but is highly toxic. The range of spirits of potable alcohol is from country spirit to whisky and the ethyl alcohol content varies between 19 to about 43 per cent. These standards are according to the ISI specifications. In other words, ethyl alcohol (95 per cent) is not alcoholic liquor for human consumption but can be used as raw material input after processing and substantial dilution in the production of whisky, gin, country liquor, etc. In many decisions, it was held that rectified spirit is not alcohol fit for human consumption. Reference may be made in this connection to Delhi Cloth and General Mils Co. Ltd. v. Excise Commissioner, U.P. Allahabad. "

14. In the case of State of Karnataka Vs. Shaw Wallace & Co. Ltd., reported in 110 STC 506, the High Court of Karnataka considered a case of the dealer engaged in Indian Made Foreign Liquor. The High Court held that without blending there cannot be any manufacture of IMFL. It is also to be pointed out that blending is also an essential part of the manufacturing process of IMFL. Even if the part of the process is done by the assessee and the other part under the control and the supervision of other parties, yet, the concept of manufacturing process cannot be taken out.

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15. We are in entire agreement with the decision of the Tribunal, which is in accordance with the law laid down by the Supreme Court on the interpretation of the concept 'manufacture'. In our view, the appeals do not deserve admission, as no interference is called for by this Court. The appeals are dismissed.

Sd/
Asst.Registrar

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Sub Asst.Registrar

mf/ksv

To:

1. The Assistant Registrar,
Income-Tax Appellate Tribunal
Rajaji Bhavan, III Floor,
Besant Nagar, Chennai - 90.

2. The Commissioner of Income Tax,
Chennai.

3. The Commissioner of Income Tax (Appeals) XI,
Chennai.

4. The Income Tax Officer,
Ward-I(1), Pondicherry.

1 cc To Mr.Pushya Sitaraman, Standing Counsel for I.T.Cases, SR.65246.

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